UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

TYCO INTERNATIONAL, LTD. and TYCO INTERNATIONAL (US), INC., Plaintiffs/Counterclaim Defendants, v. L. DENNIS KOZLOWSKI, Defendant/Counterclaim Plaintiff.	:	No. 02 Civ. 7317 (TPG) **ECF CASE**

REPLY MEMORANDUM OF LAW OF DEFENDANT/COUNTERCLAIM PLAINTIFF L. DENNIS KOZLOWSKI IN FURTHER SUPPORT OF HIS MOTION FOR PARTIAL SUMMARY JUDGMENT

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Defendant/Counterclaim Plaintiff L. Dennis Kozlowski, by his undersigned counsel, respectfully submits this reply memorandum of law in further support of his motion, pursuant to Rule 56 of the Federal Rules of Civil Procedure and Rule 56.1 of the Local Rules, for partial summary judgment on his claims against Plaintiffs/Counterclaim Defendants Tyco International Ltd. and Tyco International (US) Inc. ("Tyco") for (i) breach of the Executive Retirement Agreement, and (ii) breach of Tyco's obligation to indemnify Mr. Kozlowski in connection with Stumpf v. Garvey.

PRELIMINARY STATEMENT

As Mr. Kozlowski established in his opening brief and Tyco has conceded, on March 1, 1999, Mr. Kozlowski and Tyco entered into an Executive Retirement Agreement ("ERA") to defer payment of compensation previously earned and immediately due to Mr. Kozlowski. Under the ERA, Mr. Kozlowski agreed to defer his right to immediate payment of his bonus in return for the guaranteed right to receive a lump sum retirement benefit upon the termination of his employment, regardless of the circumstances. The contract was authorized by Tyco's Board of Directors and its terms are unequivocal: Mr. Kozlowski is entitled to immediate payment of the Lump Sum Amount "upon the termination of [his] employment with Tyco ***for any reason***."

In opposing Mr. Kozlowski's motion, Tyco attempts to raise two affirmative defenses to the payment required by this unequivocal contract. The first of Tyco's two affirmative defenses – the "faithless servant" doctrine – fails as a matter of law. Tyco asserts that New York's "faithless servant" doctrine requires disgorgement of all compensation Mr. Kozlowski earned from 1995 through 2002 and abrogates all of Mr. Kozlowski's contractual rights to payment. Tyco's argument is baseless. New York law does not apply to this claim for breach of a contract entered into between a Bermuda corporation and its CEO containing an express Bermuda choice-of-law provision. Tyco has failed to offer any legally cognizable basis to reject that contractual choice of Bermuda law, disregard well-established New York choice of law rules requiring application of Bermuda law, and apply New York law instead.

Bermuda law governs and does not permit the defense. Bermuda law, and the English common law, simply do not recognize the "faithless servant" doctrine or any equivalent. Although Tyco now attempts to rely on a fall-back argument that Bermuda and New York law are "equivalent," Tyco and its expert, Kiernan J. Bell, have not cited to a single Bermuda, English or other Commonwealth case holding that disgorgement of earned compensation is an appropriate remedy for breach of duty by an employee or officer. Nor could they. The Bermuda and English authorities to which Tyco points permit disgorgement only of certain external agent "commissions" and only in limited circumstances; they have nothing whatsoever to do with corporate officers and employees or their salaries, bonuses and other compensation. That, presumably, is why Tyco has for years struggled so mightily to avoid application of the clear Bermuda choice-of-law provision in the ERA.

Tyco's second defense to payment under the ERA – that the contract was fraudulently induced and should be rescinded – also fails. As a matter of law (i) none of the purported misrepresentations on which Tyco relies can support a claim for fraud, and (ii) Tyco has not shown and cannot show that it relied on any alleged misrepresentations because it knew the underlying truth. The criminal convictions are of no use to Tyco here. The jury in Mr. Kozlowski's criminal trial necessarily decided that as of March 1, 1999, when Tyco entered the ERA, Mr. Kozlowski had engaged in only three discrete wrongful acts, each the making of a false entry on a business record. On the undisputed facts, Tyco knew the truth underlying each of those false entries before it entered into the ERA. Nothing was concealed from the Company and none of the entries constitutes a material omission. The only other misrepresentations Tyco alleges were made solely in recitals contained in the "whereas" clauses of the ERA itself which, as a matter of Bermuda statute and common law, cannot give rise to a claim for fraud. Tyco also has failed to put forward any facts showing reliance, and because the undisputed facts demonstrate that the Company, through its own records, employees, officers and agents, knew the truth, Tyco cannot show reliance as a matter of law.

Even if the Court were to accept Tyco's untenable claim for fraud and rescind the ERA, Tyco would still owe Mr. Kozlowski the compensation deferred by that contract. Tyco admits that the ERA was entered in part to defer compensation previously earned and payable as of the date the contract was entered and amended. If the contract is rescinded and the parties returned to the *status quo ante* as Tyco demands, the amounts are still due and should be promptly paid.

Tyco also fails to provide any legally cognizable basis to reject Mr. Kozlowski's claim for indemnification for his legal fees and defense costs in Stumpf v. Garvey, a class action brought on behalf of shareholders of TyCom Ltd., Tyco's telecommunications subsidiary, asserting claims against Tyco, TyCom, Mr. Kozlowski and others related to statements in the prospectus and registration statement for TyCom's July 2000 IPO. Tyco asks this Court to conclude that because Mr. Kozlowski was convicted, he cannot bring any claim for indemnification against Tyco – not even in an action that Tyco itself has successfully argued bears ***no relation*** to the criminal convictions. Bermuda law rejects that sweeping premise. Under Tyco's Bye-Laws and the governing Bermuda statute, each claim for indemnification must be "determined on its own merits." On the merits, Mr. Kozlowski is a defendant in Stumpf on exactly the same claims as Tyco, for actions he took within his capacity as Tyco's CEO. On those undisputed facts, Mr. Kozlowski is entitled to indemnification.

ARGUMENT

I. Tyco's Opposition Suffers From The Same Cross-Cutting Legal Errors As Its Affirmative Summary Judgment Motion.

Tyco's brief in opposition to Mr. Kozlowski's motion for partial summary judgment suffers from the same two fundamental legal errors as its affirmative motion: (A) Tyco applies the wrong substantive law to Mr. Kozlowski's claim under the ERA; and (B) Tyco's motion misapplies the doctrine of collateral estoppel to its purported defenses.

A. Tyco Fails To Apply The Correct Governing Law To Mr. Kozlowski's Claim Under The Executive Retirement Agreement.

In his opening brief, Mr. Kozlowski established that his claim for breach of the ERA and Tyco's defenses to that contract claim are governed by Bermuda law, as agreed by the parties and provided by the express terms of the contract. Memorandum of Law of Defendant/Counterclaim Plaintiff L. Dennis Kozlowski in Support of His Motion for Partial Summary Judgment, dated March 5, 2010 ("Kozlowski Moving Br.") at 22-25. In opposition, Tyco makes no attempt to rebut Mr. Kozlowski's detailed legal analysis and either admits or fails to dispute each dispositive point:

- Tyco does not, and cannot, deny that New York choice-of-law rules apply to this diversity action pending in the S.D.N.Y.
- Tyco does not, and cannot, dispute that New York's choice-of-law principles strongly favor enforcement of contractual choice-of-law provisions.

- Tyco admits that the ERA provides that Bermuda law governs the parties' rights and obligations under the contract.[1]

- Tyco does not, and cannot, dispute that New York choice-of-law principles require deference to the express choice-of-law provision in the parties' contract where, as here, (i) the jurisdiction has a substantial relationship to the parties and the contract, and (ii) applying the law of the foreign jurisdiction does not violate the fundamental policies of New York. Kozlowski Moving Br. at 23.

- Tyco does not, and cannot, dispute that Bermuda has a substantial relationship to the parties and the contract, as Tyco admits that at all relevant times it was incorporated under the laws of, and had its principal place of business in, Bermuda. Tyco 56.1 Response ¶ 2.

- Tyco does not, and cannot, dispute that application of Bermuda law would not violate the fundamental policies of New York law, as applying the law of the place of incorporation in these circumstances is ***required*** by New York's internal affairs doctrine. Kozlowski Moving Br. at 23-24.

- Finally, Tyco does not – and yet again, cannot – dispute that under New York choice-of-law principles, the contractual choice-of-law provision governs both the claim for breach of contract and Tyco's affirmative defenses to that claim. Id. at 24 n.40.

The analysis is straightforward and overwhelming: under the plain terms of the contract and well-established New York choice-of-law principles, Bermuda law governs Mr. Kozlowski's claim for breach of a contract and Tyco's defenses to that claim.

Unable to offer any response under the relevant law, Tyco confines its analysis to a footnote and the cursory assertion that "New York law governs this dispute." Plaintiffs' Brief in Opposition to Defendant/Counterclaim Plaintiff's Motion for Partial Summary Judgment, dated

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[1] Statement of Material Facts Not in Dispute Submitted Pursuant to Local Rule 56.1 by Defendant/Counterclaim Plaintiff L. Dennis Kozlowski in Support of His Motion for Partial Summary Judgment, dated March 5, 2010 ("Kozlowski SUF") ¶ 12 ("Section 7.4 of the ERA provides: 'This Agreement is subject to and shall be governed by the laws of Bermuda.'"); Tyco International Ltd. and Tyco International (U.S.) Inc.'s Response to Defendant's Statement of Material Facts Not in Dispute, dated April 16, 2010 ("Tyco 56.1 Response") ¶ 12 ("Undisputed that the quotation from Section 7.4 of the ERA is accurately reproduced.").

April 16, 2010 ("Tyco Opp. Br.") at 3-4 n.2. In a parenthetical in that footnote, Tyco contends that New York law generally applies "the law of the jurisdiction where the tort occurred." Id. That tort law proposition is irrelevant to this breach of contract claim. In any event, New York deems a tort to have "occurred" where the "plaintiff is located" – in this case, Bermuda. See Odyssey Re (London) Ltd. v. Stirling Cooke Brown Holdings Ltd., 85 F. Supp. 2d 282, 292 (S.D.N.Y. 2000). Tyco's assertion that Bermuda choice-of-law principles also would apply "the substantive law of the place where the tortious conduct occurred," Tyco Opp. Br. at 3-4 n.2, is even further afield. This is a diversity action pending in New York, and it is beyond dispute that New York choice-of-law rules govern.

Tyco's contortions to avoid Bermuda law are striking (and telling). When Tyco first denied Mr. Kozlowski's claim for payment under the ERA in 2004 and 2005, it asserted that New York law governed the ERA and that New York's "faithless servant" doctrine absolved Tyco of all obligations under the contract.[2] In moving for summary judgment on the ERA claim in March 2010, however, Tyco abandoned New York law completely and insisted that ERISA and federal common law "preempt" state law and exclusively govern the ERA and Tyco's defenses. See Memorandum of Law in Support of Plaintiffs Tyco International Ltd.'s and Tyco International (US) Inc's Motion for Partial Summary Judgment on Liability and Defendants' Counterclaims, dated March 5, 2010 ("Tyco Br.") at 34 ("The ERA is an unfunded 'top hat' pension plan governed by ERISA," which "preempts all state law causes of action"); 36-38 (applying federal common law to Tyco's forfeiture and fraud defenses). Now, in its April 16, 2010 opposition, Tyco abandons the ERISA choice-of-law that it advocated in its affirmative motion, and again reverts to New York. Tyco Opp. Br. at 3-4 n.2. None of Tyco's choice-of-law analyses offer any coherent reason to reject the contractual choice-of-law provision. Tyco's failure even to settle on a consistent alternative suggests that its "choice-of-law" analysis is nothing more than a strained attempt to avoid the law of Bermuda and its rejection of the "faithless servant" doctrine. Bermuda law applies to the ERA and to Tyco's defenses for the reasons set forth above and in Mr. Kozlowski's opening and opposition briefs, and Tyco's efforts to evade it should be rejected.

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[2] See Letter from Jane F. Greenman on behalf of the Special Appeals Committee, Tyco International (US), Inc. to L. Dennis Kozlowski, dated May 13, 2004 and delivered May 17, 2004 at 2-3 (denying claims under the ERA) and Letter from Jane F. Greenman on behalf of the Special Appeals Committee, Tyco International (US), Inc. to L. Dennis Kozlowski, dated September 15, 2005 at 2-3 (denying claims under the ERA), Exhibits 36 & 41 to the Declaration of Shannon Rose Selden in Support of the Motion for Partial Summary Judgment of Defendant/Counterclaim Plaintiff L. Dennis Kozlowski, dated March 5, 2010 ("Selden Decl.").

B. Tyco Misapplies The Doctrine Of Collateral Estoppel To Mr. Kozlowski's Claims Under The Executive Retirement Agreement And For Indemnification.

Contrary to Tyco's assertions, collateral estoppel does not establish that before the ERA was entered on March 1, 1999, Mr. Kozlowski had engaged in anything remotely like "persistent looting and fraudulent concealment over a course of years" or that Mr. Kozlowski is not entitled to indemnification. See Tyco Opp. Br. at 4, 23; see also id. at 5-6, 13-17, 21. As Mr. Kozlowski established in his opposition to Tyco's motion for partial summary judgment, collateral estoppel precludes litigation only of issues that were "***necessarily decided*** in the prior proceeding." Owens v. Treder, 873 F.2d 604, 607 (2d Cir. 1989) (emphasis added); see Central Hudson Gas & Elec. Corp. v. Empresa Naviera Santa S.A., 56 F.3d 359, 368 (2d Cir. 1995) (only issues that were "essential to the judgment" are deemed to have been "actually litigated and decided" in the prior proceeding); see also Memorandum of Law of L. Dennis Kozlowski in Opposition to the

Motion of Tyco International Ltd. and Tyco International (US) Inc. for Partial Summary Judgment, dated April 16, 2010 ("Kozlowski Opp. Br.") at 4-5. In Mr. Kozlowski's criminal trial, the jury "necessarily decided" only three discrete acts that had occurred prior to March 1, 1999, each a false entry made on a business record:

- The jury necessarily decided that in or about September 1995, Mr. Kozlowski made a false entry on a relocation loan program document in that the document misrepresented that it was identical to the program "adopted by the Compensation Committee of the Board of Directors on August 1, 1995." Statement of Additional Material Facts in Dispute Submitted by Defendant/Counterclaim Plaintiff L. Dennis Kozlowski, dated April 16, 2010 ("Kozlowski SDF") ¶¶ 56, 58.

- The jury necessarily decided that Mr. Kozlowski made a false entry on a Director and Officer Questionnaire ("DOQ"), dated November 30, 1997, in that he represented that he "did not have indebtedness other than indebtedness arising from transactions in the ordinary course of business and indebtedness owed Tyco in connection with any loan granted in connection with the Company's [Key Employee Corporate Loan Program ("KELP")] owed to Tyco . . . in an aggregate amount of $60,000", when in fact he had outstanding KELP and relocation loans in excess of $60,000 allegedly taken for purposes other than those authorized by the governing programs. Id. ¶¶ 59, 61.

- The jury necessarily decided that Mr. Kozlowski made the same false entry on his November 30, 1998 DOQ. Id.

As Mr. Kozlowski demonstrated in his opposition brief, the convictions for conspiracy in the fourth degree and violation of the Martin Act ***did not*** amount to general findings of continuous misconduct and ***do not*** establish any misconduct pre-dating March 1, 1999. Kozlowski Opp. Br. at 6. Although the conspiracy indictment alleged 66 overt acts, some of which pre-dated March 1, 1999, the jury was instructed that in order to convict it had to find that Mr. Kozlowski had committed only ***one*** such overt act. Kozlowski SDF ¶¶ 74-75. Any one of the three acts underlying the business records counts would have been sufficient to support that finding. Id. ¶ 75. No other acts were "essential" to the jury's judgment on that count and, since the jury did not enter any special verdict sheet, there is no factual basis to infer that the jury "necessarily" found any additional acts. Id. ¶¶ 75-79. Similarly, although the indictment alleged a number of misrepresentations and concealments in connection with the Martin Act charge, the trial court instructed the jury that "the People need not prove every allegation contained in [the indictment]" but rather must prove only "a pattern of behavior consisting of more than isolated and unrelated acts." Id. ¶ 82. Because there is no way to determine which specific alleged acts supported the jury's verdict on the Martin Act count, and because some of the alleged acts overlapped with allegations underlying the business record counts, the jury did not "necessarily determine" that any misconduct other than the three acts discussed above had occurred prior to March 1, 1999. Id. ¶¶ 80-83. These three discrete false entries – all of which involved information otherwise available in Tyco's records and that Tyco ***knew*** at the time – are the only aspects of the conviction that pre-date the ERA. Collateral estoppel does not and cannot establish any other misconduct before the contract was entered.

II. Tyco's "Faithless Servant" Defense Fails As A Matter Of Law.

Tyco contends that New York's "faithless servant" doctrine is a complete defense to Mr. Kozlowski's claim for breach of the ERA and that it requires disgorgement of all compensation earned from 1995 through 2002. Tyco Opp. Br. at 3-13. Tyco's position is wholly without merit. As detailed above, in Section I.A, New York law does not apply.[3]

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[3] Even if New York law did apply (which it does not), Tyco's defense would fail for the numerous reasons addressed in detail in Mr. Kozlowski's opposition brief. See Kozlowski Opp. Br. at 16-17, 40-42.

Bermuda law, which Tyco has labored to avoid, does not permit the defense. Neither Tyco nor its expert, Kiernan J. Bell, cite to a single Bermuda, English or other Commonwealth case holding that disgorgement of earned compensation is an appropriate remedy for breach of duty by an employee or officer. See Affidavit of Kiernan J. Bell, dated April 13, 2010 ("Bell Aff.") ¶¶ 17-24 and authorities cited. Nor could they. Bermuda law, and the English common law, simply do not recognize the "faithless servant" doctrine or any equivalent.

Tyco's contention that Bermuda law recognizes legal principles "equivalent" to the New York "faithless servant" doctrine is entirely unsupported by the authorities on which Tyco relies. See generally Reply Declaration of Saul M. Froomkin, O.B.E., Q.C., dated May 12, 2010 ("Froomkin Reply Decl."). The authorities cited by Tyco and Ms. Bell permit disgorgement as a remedy only in limited circumstances not at issue here. Id. ¶¶ 5-11 (discussing and summarizing Bermuda and English authority). All of the cases on which Tyco relies share two distinct and common facts:

- Every one of the cases on which Tyco relies involved an external agent hired by a principal to handle a single, one-off transaction on the principal's behalf, id. ¶¶ 7-8; and

- Every one of the cases on which Tyco relies involved a claim by a principal for disgorgement of undisclosed commissions (i.e. kick-backs) that its agent allegedly received from a third-party – the counterparty on the other side of the transaction that the agent was negotiating on behalf of the principal. Id.

Tyco has not pointed to and cannot point to a single case under Bermuda or English law involving disgorgement of salary or other compensation earned by an employee or officer or earned in the context of any on-going engagement or employment relationship. Id. ¶ 7. Not a single one of the cases Tyco cites requires the repayment of ***any*** salary or compensation, much less of ***all*** salary and compensation earned over a multi-year period. Id. ¶¶ 7-8. The cases on which Tyco relies are particularly irrelevant to the ERA: none supports abrogating the express terms of a written contract, much less a contract in which the parties defined precisely the circumstances under which payment obligations would or would not arise. There is simply no comparison between the cases on which Tyco relies – seeking forfeiture of undisclosed commissions earned for single, one-off transactions – and Tyco's demand for the complete disgorgement of all salary and compensation earned over seven years for the vast array of tasks and responsibilities involved in running a multi-national conglomerate.

While Tyco asks this Court to equate Mr. Kozlowski's bonuses and compensation with the "secret profits" disgorged in these cases, it fails to explain that "secret profits" is a term of art in Bermuda and English law. Id. ¶ 9 (citing Imageview Mgmt. Ltd. v. Jack, [2009] EWCA Civ 63; Murad v. Al-Saraj, [2005] EWCA Civ 959; Hippisley v. Knee Bros., (1904) 1 K.B.1). "Secret profits" refers exclusively to (i) a commission (or kick-back) taken by an agent or other fiduciary from a commercial counterparty and (ii) not disclosed to the agent's principal. The term does ***not*** describe any and all improperly-obtained funds, and certainly does not describe salary and compensation awarded by an employer. Id. It specifically is not used to describe funds improperly obtained from the principal, but rather applies only to commissions received from a ***third party*** to the transaction and not disclosed to the principal. Id. The term ***never*** describes compensation, whether proper or improper, taken by an employee or officer from his direct employer. Id. Tyco alleges that the amounts wrongfully taken by Mr. Kozlowski were taken from his principal, Tyco, in the course of his ordinary employment: by definition, those amounts are not "secret profits" under Bermuda law. Id. Tyco has not provided and cannot provide any basis to conclude that the specific remedies available for this distinct form of misconduct by an external agent apply to Mr. Kozlowski or permit complete disgorgement of all compensation earned during his seven-year tenure as Tyco's CEO.

The discussion of Bermuda and English authorities in Tyco's opposition is misleading for another reason: although the cases deal exclusively with "commissions" earned by external agents handling a discrete assignment, Tyco insists that they warrant disgorgement of all "compensation," including Mr. Kozlowski's salary as well as bonuses he earned based on corporate performance metrics. The narrowly decided cases Tyco cites do not stand for that sweeping proposition. Id. ¶ 10. None of the claimants in the cases Tyco relies on even sought disgorgement of earned compensation from an employee, and not once did the court allow it. Id. ¶ 11. In fact, a number of the cases affirmatively illustrate that disgorgement of compensation is not a remedy available under Bermuda or English law. Id. ¶¶ 12-15 (discussing Murad v. Al-Saraj, [2005] EWCA Civ 959; Fassihi v. Item Software (UK) Ltd., [2005] 2 BCLC 91, [2004] EWCA (Civ) 1244; Keppel v. Wheeler, (1927) 1 K.B. 577). In Murad v. Al-Saraj, for example, the English Court of Appeal made clear that Mr. Al-Saraj, an agent who breached his fiduciary duties to his principals in connection with buying a hotel on their behalf, was entitled to his paid salary despite his breaches. Id. ¶ 12. The court expressly noted that the breaching fiduciary's right to earned compensation was undisputed. Id.

Fassihi v. Item Software (UK) Ltd., [2005] 2 BCLC 91, [2004] EWCA (Civ) 1244, discussed in Mr. Kozlowski's opening brief, further confirms that disgorgement of compensation is not an available remedy for breach of duty under Bermuda or English law. In Fassihi, the English Court of Appeal allowed a director who had been fired for breach of his fiduciary duties to successfully claim salary earned but not yet paid. Id. ¶ 14. Although Tyco and its expert, Ms.

Bell, attempt to undermine the relevance of Fassihi, Tyco Opp Br. at 11-12 & Bell Aff. ¶¶ 28-30, their analysis overlooks crucial elements of the decision. Ms. Bell argues, for example, that Fassihi turns on the application of "an English statute which [has] no applicability in Bermuda." Bell Aff. ¶ 28 n.4. But Ms. Bell fails to note that Bermuda has an identical statute, which its courts interpret according to the English precedent. Froomkin Reply Decl. ¶ 16 (comparing the English *Apportionment Act 1870* to the Bermuda *Rent Apportionment Act 1880*). In interpreting their own statute, Bermuda courts follow the English precedent, including Justice Holman in Fassihi who explains:

> "In my view, even in the case of dismissal for misconduct, it is not right that the employee should be deprived of remuneration for work actually done; although he may be liable to his employer for damages flowing from his misconduct. … In short, an employee whose employment terminated during a pay period is entitled under the Act to apportioned salary irrespective of the cause of termination."

Id. ¶ 17.

Tyco's attempt to minimize the importance of Fassihi – and of Justice Holman's conclusion – by arguing that Justice Arden, writing on the same panel in the same case, expressed "no view" on the payment of salary does not diminish the importance or relevance of Justice Holman's opinion or of Fassihi. Justice Arden may have remained silent but there was no reason for her to speak: the court below had found for Mr. Fassihi on this very issue and the company had elected not to appeal. Id. ¶ 18. The failure to appeal on that issue is itself revealing – if English law included anything approaching the "faithless servant" doctrine, the injured employer in that case surely would have invoked the doctrine in both courts and added the argument to its appeal. It did not, and the lower court's decision affirming Mr. Fassihi's right to earned salary stands. Id. Justice Arden's silence is irrelevant for the additional reason that Justice Holman delivered the opinion of the court and addressed the subject in detail, agreeing with the lower court that Mr. Fassihi was entitled to keep the salary he had earned. Id.

Tyco's last attempt to distinguish Fassihi v. Item Software from this dispute, by contrasting it to Murad v. Al-Saraj, fails as well. See Bell Aff. ¶ 30. Fassihi and Murad reach exactly the same result with regard to paid compensation: in each, the breaching fiduciary was allowed to keep the compensation he had earned. Froomkin Reply Decl. ¶¶ 19-20. Indeed, the plaintiffs in neither case even made a claim for the disgorgement of such compensation. Id. ¶ 20. These two recent decisions by differently constituted Courts of Appeal in England do not even contemplate the possibility that a defaulting fiduciary should forfeit earned salary to the company. Id. Murad and Fassihi provide a far more accurate statement of English and Bermuda law than Tyco or its expert. Those cases illustrate that the common law of England and Bermuda recognize nothing close, let alone "equivalent," to Tyco's "faithless servant" defense. Id.

III. Tyco's Fraudulent Inducement Defense And Demand For Rescission Fail As A Matter Of Law.

Tyco's argument that the ERA is not enforceable and should be rescinded because it was fraudulently induced fails for two reasons: (i) none of the purported misstatements on which Tyco relies support a claim for fraud, and (ii) Tyco could not have relied on the alleged misrepresentations or omissions because it knew the underlying truth.

A. Tyco Has Not Identified Any Actionable Misrepresentations Regarding The ERA.

Tyco has failed to offer any evidence of actionable affirmative misrepresentations by Mr. Kozlowski seeking to induce Tyco to enter the ERA. Instead, Tyco points exclusively to the prefatory statements in the ERA itself and incorrectly asserts that the contract itself contains actionable "false statement[s] of present fact." Tyco Opp. Br. at 16, 18. Specifically, Tyco points to recitals in the "whereas" clauses of the ERA to argue that "[b]y signing the ERA with this statement of intention, Kozlowski made two knowingly false representations of material fact: (i) that he had been loyal to Tyco prior to March 1, 1999; and (ii) that he intended to be loyal to Tyco following the execution of the ERA." Id. at 16. Neither type of alleged misrepresentation can support a claim for fraud.

Bermuda law governs, see supra Section I.A, and Bermuda law does not permit the claim. Bermuda and England have identical statutes defining actionable misrepresentations, which require a misrepresentation to have occurred ***before*** the contract is entered to be actionable. Froomkin Reply Decl. ¶¶ 23, 25. Under those statutes and under the common law of England, as followed in Bermuda, "a present intention not to perform on a contract cannot give rise to a claim for misrepresentation." Id. ¶ 24. Bermuda's definitive treatise on actionable misrepresentations confirms that "he who sues on a contractual promise, as if it were a representation, must fail." Id. (citing Spencer Bower, Turner, Handley, Actionable Misrepresentation ¶ 21 (4th ed. London 2000)). Under this unequivocal Bermuda law, the recitals in the ERA cannot and do not support Tyco's claim for fraudulent inducement.

Tyco's contention that Mr. Kozlowski misrepresented his "intent to perform" under the ERA fails for the additional reason that the ERA does not impose any such performance obligation. Section 1.1 of the ERA – the first operative paragraph of the contract – states that "[n]otwithstanding anything herein contained to the contrary, ***this Agreement is not an agreement of employment*** . . . ." Kozlowski SUF ¶ 6 (ERA § 1.1) (emphasis added). The ERA does not give Mr. Kozlowski any right or obligation to employment by Tyco and does not impose on Tyco any right or obligation to employ Mr. Kozlowski. See id. The ERA does not impose any performance obligations and expressly does not condition payment on loyalty. See id. Rather, the ERA is an agreement by Tyco to pay Mr. Kozlowski, or his beneficiary, a specified Lump Sum Amount when one of three things happens: (i) he retires, (ii) his employment is terminated "for any reason," or (iii) he dies prior to retirement or termination. Id. ¶¶ 7-11 (ERA §§ 2, 3 & 4). By its plain terms, the ERA did not require Mr. Kozlowski to "perform" or to "remain loyal" to the Company. It is indisputable that, under the clear and unambiguous terms of the contract, Mr. Kozlowski could have quit the next day after signing the ERA and still be entitled to the Lump Sum Amount.

It is evident from the plain language of the ERA and its admitted purpose that statements, if any, regarding Mr. Kozlowski's performance under the ERA are immaterial. Tyco admits that the ERA was primarily a mechanism to defer the payment of compensation that Mr. Kozlowski ***already had earned***. Tyco 56.1 Response ¶ 5; Kozlowski SUF ¶ 5 ("The Executive Retirement Agreement deferred a portion of the bonus earned in and otherwise payable to Mr. Kozlowski for fiscal year 1998."). The amounts deferred were determined by Mr. Kozlowski's past performance, as reflected in the Company's strong results and measured by Tyco's long-standing incentive formula.[4] The 1999 amendment to the ERA was entered for the same reason. Tyco does not dispute that the Company's 1999 results again produced a substantial bonus for Mr. Kozlowski, when Tyco reported over $22.4 billion in net revenues and exceeded its targets for earnings per share, pretax income and operating cash flow.[5] Nor does Tyco dispute that Mr. Kozlowski was entitled to receive that bonus immediately. Kozlowski Moving Br. at 9-10. Tyco does not and cannot deny that Mr. Kozlowski agreed to forgo immediate payment of that 1999 bonus in favor of deferred payment pursuant to an amendment to the ERA.[6] In fact, Tyco concedes that it agreed to that amendment to the ERA in October 1999.[7] Tyco 56.1 Response ¶ 9. While Tyco argues that it would not have agreed to the amendment "had it been aware" of the alleged disloyalty and fraud, id., it never denies that the primary purpose of that amendment was to defer compensation that Mr. Kozlowski ***had already earned*** as a performance bonus for 1999. Kozlowski Moving Br. at 10. While the amount due under the ERA exceeds the total deferred compensation, the ERA confirms that the right to payment of the entire "Lump Sum Amount" was fully ripe at the moment the agreement was entered: it states that the amount due has "fully vested" and must be paid upon termination of employment "for any reason." Kozlowski SUF ¶ 11 (ERA § 4.1). On these undisputed facts, Tyco has not raised and cannot raise any inference that statements, if any, regarding Mr. Kozlowski's loyalty or intent to perform under the ERA were material to the contract.

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[4] Selden Decl., Ex. 31, Transcript of Deposition of Stephen Foss, dated May 11, 2007 ("Foss Dep. Tr."), at 666:14-668:24, 674:5-675:22.

[5] Selden Decl., Ex. 31, Foss Dep. Tr. at 666:14-668:24, 674:5-675:22; Selden Decl., Ex. 15, Tyco Int'l Ltd, Annual Report (Form 10-K), at 32 (Dec. 13, 1999); see also Selden Decl., Ex. 19, Tyco Int'l Ltd., Annual Report (Form 10-K/A), at 26 (July 29, 2003) (restating 1999 revenues as $22,494.1 billion, net income as $873.7 billion and per share earnings of $0.53).

[6] Selden Decl., Ex. 31, Foss Dep. Tr. at 674:5-675:9, 667:14-18, 675:14-676:9, 668:1-10.

[7] Selden Decl., Ex. 1, ERA at First Amendment ¶ A.

As these undisputed facts establish, even if the Court were to grant Tyco's request for rescission of the ERA, Mr. Kozlowski would still be entitled to payment of his deferred compensation. Tyco concedes that the ERA was entered to defer compensation previously earned and payable as of the date the contract was entered and amended. If the contract is rescinded and the parties returned to the *status quo ante* as Tyco demands, the amounts are still due and should be promptly paid.

B. Tyco's Fraudulent Inducement Defense Fails Because Tyco Cannot Establish Reliance As A Matter of Law.

Tyco's assertion of fraudulent inducement and demand for rescission also fail as a matter of law because Tyco has not identified and cannot identify any material facts showing reliance. Under Bermuda law, as under New York law (which does not apply), reliance on the alleged misrepresentation is an essential element of fraudulent inducement. Froomkin Reply Decl. ¶¶ 23, 27. To show reliance, "Tyco must show that it did not know that the misrepresentations in question were untrue." Id. ¶ 27. English law, which Bermuda follows, recognizes as a matter of horn-book law that a party cannot state a claim for fraud where it had knowledge of the truth. Id. ¶¶ 27-34 (citing authorities). In the corporate context, "the knowledge of an agent acquired in service of his principal will be imputed to his principal" and, accordingly, the knowledge of Tyco's agents and employees is imputed to Tyco. Id. ¶ 29 (citing case law and treatise). The reliance must precede the contract – i.e., Tyco must have relied on misrepresentations ***before*** it entered the ERA. Id. ¶¶ 23, 25. Accordingly, the criminal convictions based on conduct that occurred ***after*** the ERA was entered are irrelevant. Id. ¶ 25. Applying that bright-line rule, only the three business records convictions addressed above could have any bearing on the ERA. See supra Section I.B. Even those convictions cannot establish reliance, however, because the undisputable facts demonstrate that Tyco knew about the underlying conduct. In short, Tyco has not put forward a single fact sufficient to show it relied upon any alleged misrepresentations before entering the ERA on March 1, 1999.

Instead of coming forward with facts showing actual reliance on an alleged misrepresentation or omission, Tyco engages in a striking bit of circular reasoning: it asks this Court to find that *because it entered the ERA*, it must have been misled into doing so. Specifically, Tyco points to the ERA's "whereas" clauses as proof of reliance, arguing that the "recital shows that Tyco was made to believe that Kozlowski had been in the past and intended to be in the future a loyal fiduciary" and that based on these representations, Tyco "agreed to the ERA." Tyco Opp. Br. at 19-20. The recital shows no such thing. As discussed above, a statement made in a contract is not an actionable misrepresentation and cannot, as a matter of law, have been relied upon as an inducement to enter the ERA. See Froomkin Reply Decl. ¶¶ 24-25. In addition, Tyco offers no testimony, document, or other factual basis to infer that it ever relied on any other alleged misrepresentation prior to entering the ERA, much less what that specific representation was. Tyco cannot establish reliance by pointing to the fact that, in the end, it signed the contract. The fact that a party elected to enter a contract is not, standing alone, sufficient to raise an inference that the contract was fraudulently induced.

Tyco's attempt to use Mr. Kozlowski's criminal convictions to establish reliance is without merit. See Tyco Opp. Br. at 19-20. Tyco's lack of knowledge of the conduct was not an element of any of the crimes for which Mr. Kozlowski was convicted, nor was Tyco's reliance on any alleged misrepresentation. Kozlowski SDF ¶¶ 13, 54-55, 74, 80-81. Tyco argues that "[h]ad [it] been aware of Kozlowski's ongoing criminal activity prior to March 1999, . . . Kozlowski would never have secured the benefits of the ERA." Tyco Opp. Br. at 20. But the only evidence Tyco introduces to support this critical proposition is the fact that, three years later, "after learning of Kozlowski's imminent indictment for sales tax evasion, the Tyco Board requested and obtained Kozlowski's resignation[]." Tyco International Ltd. and Tyco International (US) Inc.'s Statement of Undisputed Facts, dated March 5, 2010 ¶ 6; Tyco Opp. Br. at 20. Tyco's 2002 response to an imminent public indictment concerning completely unrelated conduct – which was alleged to have occurred in late 2001 and 2002 – does not, and as a matter of logic cannot, establish reliance on an alleged fraudulent omission made more than three years earlier, in or before March 1999.

Moreover, Tyco has failed to introduce any evidence to show that it was in fact ignorant of any criminal activity prior to March 1999. Tyco Opp. Br. at 20. Tyco does not point to a single deposition or affidavit to support its claim of ignorance. Instead, Tyco simply asks this Court to infer from the fact that it entered the ERA that the Company did not know about any misconduct and relied on an assumption that none existed. That is not enough to defeat a claim for summary judgment. Because Tyco has not come forward with any specific facts showing that it did not know the truth – i.e., that it was unaware of the "criminal activity prior to March 1999" – it cannot establish reliance on the purported misrepresentation. Its claim for fraud fails and Mr. Kozlowski's motion should be granted.

Tyco's silence on this point is not surprising. Tyco cannot introduce any facts to show it did not know of the misconduct because the facts show it ***did*** know. As Mr. Kozlowski has demonstrated, voluminous evidence establishes that Tyco officers, employees and agents knew about the conduct underlying the only three convictions that pre-date the March 1999 ERA, which relate to (i) a relocation loan program document, (ii) the 1997 DOQs, and (iii) the 1998 DOQs. The facts are beyond dispute:

- Relocation Program: Tyco officers and lawyers, including Tyco's Treasurer Barbara Miller and in-house attorney Brian Moroze, drafted and reviewed the purportedly false September 1995 relocation loan program document associated with Mr. Kozlowski's business record conviction and knew that it was not "identical" to the program adopted by the Board. Kozlowski Opp. Br. at 21-22; Kozlowski SDF ¶¶ 58(a)-(d). ***Both documents were kept in Tyco's company records and available for review at any time***. Kozlowski SDF ¶ 58(c); Exhibits 50-53 to the Declaration of Shannon Rose Selden in Support of the Opposition of L. Dennis Kozlowski to the Motion by Tyco International Ltd. and Tyco International (US) Inc. for Partial Summary Judgment.
- 1997 DOQs and 1998 DOQs: ***The information that Mr. Kozlowski was convicted of failing to disclose*** on his November 30, 1997 and November 30, 1998 DOQs ***was available in Tyco's own documents and records***. Kozlowski Opp. Br. at 20-21; Kozlowski SDF ¶¶ 61-70. In addition, Tyco, and its officers, directors and agents, were aware of the purportedly undisclosed KELP and relocation borrowings. Kozlowski Opp. Br. at 20-22; Kozlowski SDF ¶¶ 61-70. In many instances, Tyco officers and agents, including Senior Vice President and Treasurer Michael Robinson and Executive Treasury Department employee Kathleen McRae, facilitated those borrowings by requesting and approving wire transfers charged to Mr. Kozlowski's KELP and relocation loan accounts for purchases and investments of a personal nature that were allegedly unauthorized under the governing loan programs. Kozlowski SDF ¶¶ 62, 64.

As a matter of Bermuda law, Tyco's own documents and the knowledge of Tyco's employees, officers, and agents are the knowledge of the Company.[8] Froomkin Reply Decl. ¶¶ 27-29. Because Tyco knew the truth, it could not have relied on the omission. Id.

The same is true under New York law, which does not apply but on which Tyco nonetheless relies. As Mr. Kozlowski demonstrated in his opposition to Tyco's motion for partial summary judgment, under New York law, "a party cannot demonstrate justifiable reliance on representations it knew were false." Merrill Lynch & Co. Inc. v. Allegheny Energy, Inc., 500 F.3d 171, 182 (2d Cir. 2007) (citation omitted); see also Banque Franco-Hellenique de Commerce Int'l et Mar., S.A. v. Christophides, 106 F.3d 22, 26-27 (2d Cir. 1997). A corporation, therefore, "cannot rely on misrepresentations unless its agents or employees rely on those misrepresentations." Bank of China, N.Y. Branch v. NBM LLC, 359 F.3d 171, 179 (2d Cir. 2004). If a corporation's officers and employees are aware of the alleged fraud, their knowledge is imputed to the corporation. Id. As the Second Circuit put it, "if the [company's] officers were aware of, and participated in the defendants' allegedly fraudulent activities, then neither they, ***nor the [company]*** relied on the purported misrepresentations." Id. at 179 (emphasis in original); see also Banco de Chile v. Lavanchy, No. 05 Civ. 4658 (GBD)(KNF), 2008 U.S. Dist. LEXIS 91499, at *22-23 (S.D.N.Y. Nov. 6, 2008) (corporation precluded from establishing reasonable reliance when general manager facilitated scheme). Under New York law, as under Bermuda law, Tyco cannot show reliance.

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[8] Tyco has not pursued claims for fraud or other misconduct against these employees, officers, and agents, several of whom remained with the Company, although it has long been aware of their knowledge and roles. Kozlowski SDF ¶¶ 123-24.

In short, Tyco has not come forward with any specific facts sufficient to challenge the validity of the ERA or to establish a right to rescission based on fraudulent inducement. Even if it had, rescinding the contract would not eliminate the underlying obligation to pay Mr. Kozlowski's 1998 and 1999 bonuses, which were due, owing, and deferred for payment via the ERA.

IV. Tyco Is Required To Indemnify Mr. Kozlowski For Stumpf v. Garvey.

Tyco's opposition to Mr. Kozlowski's claim for indemnification, like Tyco's affirmative motion for summary judgment, depends on an egregious overstatement of the collateral consequences of his criminal conviction. Tyco's position is not supported by Bermuda law and cannot defeat Mr. Kozlowski's narrowly tailored motion for indemnification.

Tyco's opposition to indemnification hangs entirely on its contention that the criminal convictions preclude Mr. Kozlowski's claim for indemnification from Tyco, either under the Bye-Laws or because Mr. Kozlowski has "unclean hands." See Tyco Opp. Br. at 24. Neither theory is correct. A criminal conviction does not prevent a party from asserting contractual indemnification rights under Bermuda law. Froomkin Reply Decl. ¶ 38. The claim for indemnification must be "determined on its own merits" and is not extinguished by the criminal convictions. Id. Similarly, Tyco's argument that Mr. Kozlowski cannot obtain indemnification because he has "unclean hands" is not supported by the authorities it cites, or by Bermuda law. Where Tyco's expert, Ms. Bell, relies on Snell's Equity for the proposition that "he who comes into equity must come with clean hands," Bell Aff. ¶ 42, she omits the conclusion of the quoted paragraph, which states that "The maxim must not be taken too widely: 'Equity does not demand that its suitors shall have led blameless lives.' What bars the claim is not a general depravity but one which has an 'immediate and necessary relation to the equity sued for and is not balanced by any mitigating factors.'" Froomkin Reply Decl. ¶ 42 (internal citations omitted).

Here, Mr. Kozlowski is seeking indemnification for a case that Tyco itself has successfully argued bears ***no relation*** to the accusations of looting. See Stumpf v. Garvey, No. 03 Civ. 1532 (PB), 2006 WL 39237, at *1 (D.N.H. Jan. 6, 2006). Tyco's contention that the *plaintiffs* in the Stumpf case argue that the looting is relevant, Tyco Opp. Br. at 26-28, is beside the point. Tyco is bound by its own admissions that Stumpf is entirely remote from the criminal convictions. Simon v. Safelite Glass Corp., 128 F.3d 68, 71-72 (2d Cir. 1997) (judicial estoppel prevents a party from taking a position contrary to that taken in an earlier proceeding where the court had accepted the claim by rendering a favorable decision). Tyco cannot invoke the plaintiffs' (unsuccessful) argument to evade its own admissions as to the facts or its own obligations under the Company's Bye-Laws. See Kozlowski Moving Br. at 32.

Tyco's remaining arguments are equally unavailing. Tyco's contention that the claim is not ripe is inconsistent with its indemnification of numerous other Company officers and directors in litigation over the past eight years, and with the plain language of Tyco's Bye-Laws. The Bye-Laws provide that "Every Director . . . shall be indemnified by the Company against . . . all costs, losses and expenses which any such officer *may incur or become liable to*." Kozlowski SUF ¶ 27 (Bye-Laws § 102) (emphasis added); Froomkin Reply Decl. ¶ 39. The Bye-Laws thus expressly contemplate indemnification for future liabilities as well as final judgments. Froomkin Reply Decl. ¶ 39. After eight years of litigation and defense costs, Mr. Kozlowski's claim is more than ripe. Tyco's alternate theory – that the claim is not unripe, but too late because Mr. Kozlowski is entitled only to advancement – makes even less sense. Tyco's Bye-Laws do not distinguish "advancement" from "indemnification" and plainly permit the latter here. Id. ¶ 40. Moreover, Tyco's refusal to meet its advancement obligations cannot justify its failure to meet its obligation indemnify Mr. Kozlowski for the legal costs he has incurred in defending himself in this completely unrelated action.

CONCLUSION

For the reasons stated above and in his Memorandum of Law in Support of His Motion For Partial Summary Judgment, Mr. Kozlowski respectfully requests that the Court grant his motion for partial summary judgment that Tyco (i) has breached the Executive Retirement Agreement and is required to pay him the Lump Sum Amount under that contract, and (ii) is required to indemnify Mr. Kozlowski for his costs and expenses in Stumpf v. Garvey.

Dated: New York, New York
May 14, 2010

Respectfully submitted,
DEBEVOISE & PLIMPTON LLP

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